

Letter of Findings: 01-20191070
Indiana Individual Income Tax
For The Tax Years 2015, 2016, and 2017

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Individuals were responsible for additional Indiana income tax for the 2015, 2016, and 2017 tax years because, after a cross-reference examination with the Department's withholding tax records, the records reflected that Individuals overstated their county withholding tax credits.

ISSUE

I. Indiana Individual Income Tax - County Withholding Tax Credits.

Authority: IC § 6-3-1-3.5; IC § 6-3-2-1; IC § 6-3-3-3; IC § 6-3.5-6-23; IC § 6-8.1-5-1; IC § 6-8.1-5-2; [45 IAC 3.1-1-76](#); *Comptroller of Maryland v. Wynne*, 135 S. Ct. 1787 (2015); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Miller Brewing Co. v. Indiana Dep't of State Revenue*, 903 N.E.2d 64 (Ind. 2009); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2012); Income Tax Information Bulletin 28 (May 2012); Income Tax Information Bulletin 28 (November 2016); Commissioner's Directive 57 (July 2016); Income Tax Information Bulletin 115 (November 2017).

Taxpayers protest the Department's individual income tax assessments for 2015, 2016, and 2017.

STATEMENT OF FACTS

Taxpayers (Husband and Wife) are Indiana residents. Husband works for an employer in Kentucky. Each year, Taxpayers file a married-filing-jointly Indiana Full-Year Resident Individual Income Tax Return (Form IT-40), reporting their Indiana and local income tax and claiming a refund of overpayment. Taxpayers timely filed their IT-40 returns for 2015, 2016, and 2017 ("Tax Years at Issue"). The Indiana Department of Revenue ("Department") processed their returns and issued refunds pursuant to Taxpayers' filings.

In 2019, the Department conducted an examination of Taxpayers' filings for the Tax Years at Issue and cross-referenced withholding tax information in its records. The Department found that there was zero (\$0) county withholding tax for Taxpayers for the Tax Years at Issue and that Taxpayers overstated their county withholding tax credits on their Schedule 5 for all three years. The Department adjusted Taxpayers' claimed county withholding tax credits on their Schedule 5 for those years. Upon a further examination, the Department also concluded that Husband's Kentucky employer withheld the local tax and remitted to Kentucky where Husband worked. Therefore, on the Schedule 6, the Department proceeded to credit Taxpayers the full amount of their Indiana county tax as permitted by the Indiana law. The Department explained "line-by-line change or changes" and assessed additional tax, penalty, and interest as a result.

Taxpayers protested the assessments, submitting additional documentation - including copies of their "W-2 Wage and Tax Statement" for those years ("W-2 Statements"). Taxpayers requested that the Department make its final determination without a hearing. This Letter of Findings ensures based on Taxpayer's documents and information available within the Department's records. Additional facts will be provided as necessary.

I. Indiana Individual Income Tax - County Withholding Tax Credits.

DISCUSSION

After cross-referencing the Department's records and examining Taxpayers' filings for the Tax Years at Issue, the Department determined (1) that there was zero (\$0) county withholding tax remitted to the Department on Taxpayers' behalf, (2) that Taxpayers overstated their withholding tax credits for those years, and (3) that Taxpayers owed additional income tax based on their IT-40 returns for the Tax Years at Issue. The Department thus made "line-by-line" adjustments and assessed Taxpayers additional income tax, penalty, and interest pursuant to IC § 6-8.1-5-2.

Taxpayers disagreed. In their March 9, 2019, protest letter, Taxpayers asserted, in relevant part, that:

Line 12 [on the line-by-line change or changes assessment] lists only the state withholding amounts. As evident in each year's Schedule 5 Local tax was also withheld but not accounted for in the "Adjusted" column. We assume that the reciprocal agreement between Indiana and Kentucky accounts for both withholdings.

In this instance, Husband has worked for a Kentucky company and his Kentucky employer has withheld taxes - both state and local taxes - on wages paid to Husband.

The issue thus is whether Taxpayers demonstrated that they correctly filed their Indiana IT-40 returns for the Tax Years at Issue and that the assessments were wrong.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007); *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012). "[E]ach assessment and each tax year stands alone." *Miller Brewing Co. v. Indiana Dep't of State Revenue*, 903 N.E.2d 64, 69 (Ind. 2009). Thus, the taxpayer is required to provide documentation explaining and supporting their challenge that the Department's assessment is wrong. Poorly developed and non-cogent arguments are subject to waiver. *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480, 485 n.9 (Ind. Tax Ct. 2012).

Indiana imposes a tax "upon the adjusted gross income of every resident person, and on that part of the adjusted gross income derived from sources within Indiana of every nonresident person." IC § 6-3-2-1(a). To efficiently and effectively compute what is considered the resident-taxpayer's Indiana income tax, the Indiana statute refers to the Internal Revenue Code. IC § 6-3-1-3.5(a) provides the starting point to determine the taxpayer's taxable income and to calculate what would be his or her Indiana income tax after applying certain additions and subtractions to that starting point, with modifications thereafter.

In addition, Indiana has entered reciprocal agreements with several states. Under the agreed reciprocity, Indiana resident-taxpayer who earns "income consisting of salaries, wages, and commissions from states [such as, Kentucky,] with which Indiana has a reciprocal tax agreement must report all such income as if it were from Indiana." [45 IAC 3.1-1-76](#). Reciprocity, however, does not apply and automatically transfer the withholding tax credits between reciprocal states. Specifically, the same regulation provides, "**Credit cannot be taken for any taxes withheld by or paid to any of these states in connection with salaries, wages, or commissions received from such states. If tax has been withheld by any of these states, a claim for refund should be filed with the state which withheld the taxes.**" *Id.* (Emphasis added).

Indiana law also permits Indiana resident-taxpayer to claim an income tax credit - not exceeding their Indiana income tax due - for the taxes he or she is required to pay to other states. IC § 6-3-3-3(a). Similarly, when the resident-taxpayer of an Indiana county is required to pay local income tax to a county of another state, the Indiana resident-taxpayer is entitled to a tax credit. IC § 6-3.5-6-23(a) (in effect during the Tax Years at Issue) specifically provided:

Except as provided in subsection (b), if for a particular taxable year a county taxpayer is liable for an income tax imposed by a county, city, town, or other local governmental entity located outside of Indiana, that county taxpayer is entitled to a credit against the county option income tax liability for that same taxable year. **The amount of the credit equals the amount of tax imposed by the other governmental entity on income derived from sources outside Indiana and subject to the county option income tax.** However, **the credit provided by this section may not reduce a county taxpayer's county option income tax liability to an amount less than would have been owed if the income subject to taxation by the other governmental entity had been ignored.** (Emphasis added).

To claim this tax credit, the Department accepts "[w]ithholding statements or other evidence of tax payment . . . if

no return is required to be filed with the locality outside Indiana." Income Tax Information Bulletin 28 (May 2012), 20120530 Ind. Reg. 045120250NRA (explaining further that "[t]he allowable credit is equal to the lesser of: [1] [t]he amount of income tax actually paid to a locality in another state; [2] [t]he amount of adjusted gross income taxed by the locality outside of the State of Indiana multiplied by the county rate to which the taxpayer is subject; or [3] [t]he amount of county tax due on the Indiana return"); see also Income Tax Information Bulletin 28 (November 2016), 20161228 Ind. Reg. 045160560NRA.

Following the test established by the United States Supreme Court in *Comptroller of Maryland v. Wynne*, 135 S. Ct. 1787 (2015) and concluding that Indiana tax system satisfies the constitutional requirements, the Department's Commissioner's Directive 57 (July 2016), 20180131 Ind. Reg. 045180053NRA, further explains, in relevant part, as follows:

II. ANALYSIS

...

Indiana [] maintains symmetry in allowing credits at both the state-to-state level and the county-to-county level. Indiana does not permit out-of-state state income taxes to offset Indiana county income taxes or allow out-of-state local income taxes to offset Indiana state income taxes. In Indiana, [] each county chooses whether to impose a county-level income tax, and each county's governing bodies must independently approve both the tax and the rate

Although Indiana does not permit out-of-state state income taxes to offset local county income taxes, Indiana's tax system is internally consistent. Indiana allows both state-to-state and county-to-county credits. . . .

See also Income Tax Information Bulletin 115 (November 2017), 20180131 Ind. Reg. 045180053NRA.

Accordingly, the Indiana tax system encompasses different types of tax credits which include refundable tax credits and nonrefundable tax credits. Withholding tax credits are refundable while the tax credits for tax paid to other states or counties of other states are nonrefundable. When an Indiana resident-taxpayer who works in a county of another state, which has a reciprocal agreement with Indiana (such as Jefferson County, Kentucky), the Indiana resident-taxpayer must report his or her W-2 income from Kentucky on his or her IT-40 return and vice versa. Only when the employer withholds and remits the withholding taxes to Indiana, is the resident-taxpayer entitled to claim the withholding tax credit on the Schedule 5 of his or her IT-40 return. When the employer fails to do so, the resident-taxpayer has no withholding tax credits for filing IT-40 returns purposes regardless of the source of income. Reciprocity is irrelevant in claiming the withholding tax credits.

The Indiana resident-taxpayer may also claim a tax credit for local income tax paid to a county of another state. Unlike the withholding tax credits on Schedule 5, this tax credit for income tax paid to a county of another state (claimed on the Schedule 6) is not a refundable credit. This tax credit - to the extent of "[t]he amount of county tax due on the Indiana return" - is against their Indiana county income tax owed. That is, if the amount of income tax the resident-taxpayer paid to a county of another state *exceeds* the county income tax he or she would have owed under his or her Indiana return, the resident-taxpayer owes no Indiana county income tax. The resident-taxpayer receives no refund of the overpayment from Indiana on that income even when he or she has paid more tax to the county of another state.

In this instance, upon review, Taxpayers' reliance on their W-2 Statements and their application of states' reciprocity is misplaced. In particular, pursuant to the reciprocity, Taxpayers here, as Indiana residents, were required to file IT-40 returns, reporting Husband's wage income from Kentucky. Taxpayers were not required to file Kentucky income tax returns reporting Husband's Kentucky income tax.

The reciprocity however does not apply to withholding tax credits among reciprocal states. As mentioned earlier, these withholding tax credits are state specific. Taxpayers' W-2 Statements demonstrated that Husband's Kentucky employer withheld and remitted state withholding taxes to Indiana. But, it did not do so with regards to the local or county withholding taxes. Rather, Taxpayers' W-2 Statements showed that Husband's Kentucky employer withheld and remitted the local taxes to Jefferson County in Kentucky. As mentioned earlier, "[c]redit cannot be taken for any taxes withheld by or paid to any of these states in connection with salaries [or] wages [] received from such states. If tax has been withheld by any of these states, a claim for refund should be filed with the state which withheld the taxes." [45 IAC 3.1-1-76](#). In other words, Indiana did not receive the claimed county withholding tax (in the total amount of approximately \$3,480) from Husband's Kentucky employer. Therefore, there were no county withholding tax credits available to be claimed on Taxpayers' Schedule 5 to IT-40 returns for those years. If there is a remedy, it is with Kentucky.

Finally, it should be noted that, pursuant to IC § 6-3.5-6-23(a) and the *Wynne* decision, the Department properly computed and granted Taxpayers the tax credits, in the total amount of \$1,974, based on Taxpayers' W-2 Statements and their IT-40 as filed, for the county tax presumably paid to Jefferson County, Kentucky. The \$1,974 tax credits represent Taxpayers' Indiana county income taxes for those years.

In short, given the totality of the circumstances, Taxpayers' supporting documentation failed to demonstrate that the proposed assessments were wrong. The Department correctly adjusted Taxpayers' IT-40 returns to comport with the records.

FINDING

Taxpayers' protest is respectfully denied.

August 20, 2019

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An [html](#) version of this document.